



State of West Virginia
Office of the Attorney General

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December 11, 2015

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Dr. Michael J. Martirano
State Superintendent of Schools
1900 Kanawha Boulevard East, Building 6
Charleston, WV 25305

Dear Superintendent Martirano:

You have asked for an Opinion of the Attorney General regarding whether the West Virginia Department of Education ("WVDE") may directly repay a private loan taken by the Fayette County Board of Education ("County Board") using funds from the County Board's portion of state aid to schools. This Opinion is being issued pursuant to West Virginia Code § 5-3-1, which provides that the Attorney General "shall give written opinions and advice upon questions of law . . . whenever required to do so, in writing, by . . . any other state officer, board or commission." To the extent this Opinion relies on facts, it is based solely upon the factual assertions set forth in your correspondence with the Attorney General's Office.

In your letter, you explain that the Fayette County Board of Education is seeking funding for its Comprehensive Educational Facilities Plan in order to consolidate schools and facilitate new school construction. Working with a private financial advisor, the County Board is considering entering into a 15 year \$11 million lease-purchase agreement with a financial institution to fund its project. The financial institution would take a security interest in any equipment or fixtures purchased with the loan funds. You note that the loan would have an "annual funding opt-out clause." You also explain that the financial advisor has informed the County Board that the County Board could obtain a slightly lower interest rate if the WVDE pays the financial institution directly from state aid allocated to the County Board by the Legislature. According to your letter, the financial advisor has further said that the WVDE's direct involvement would "provide reassurance to potential lenders." Under the contemplated arrangement, the WVDE would not take on the County Board's liability for the loan, but rather would "function similar to a mortgagee paying insurance premiums and property tax on behalf of the mortgagor from an escrow account."

Your letter raises the following legal question:

Does the West Virginia Department of Education have the authority to direct to a financial institution state aid allocated to a county in order to repay a loan obtained from that financial institution by the county board of education?

Having reviewed controlling case law of the West Virginia Supreme Court of Appeals, we believe that the high court would find that two provisions of the West Virginia Constitution prohibit the WVDE from directly repaying a county board of education's loan using state aid to schools.

To begin, we think it likely that the Supreme Court of Appeals would find the contemplated arrangement to be a violation of Article X, Section 6 of the West Virginia Constitution. That provision states that "[t]he credit of the state shall not be granted to, or in aid of any county, city, township, corporation or person; nor shall the state ever assume, or become responsible for the debts or liabilities of any county, city, township, corporation or person." W. Va. Const. Art. X, § 6. At the very minimum, the Supreme Court of Appeals has explained, that provision bars the State or its agencies from extending to a county the State's power to borrow money. Put another way, the State "may not grant its credit in aid of counties and municipalities in negotiating loans." *State ex rel. Charleston v. Sims*, 132 W. Va. 826, 843, 54 S.E.2d 729, 739 (1949). Yet that appears to be precisely what is intended here. The State is certainly not *necessary* to the contemplated loan; the County Board could receive its state aid from the WVDE as it always has and then itself pay that money to the financial institution. The only reason for involving the State as a direct payor to the financial institution, your letter represents, is to leverage the State's credit. As you explain, the County Board's financial advisor "believes that [the WVDE's involvement] would lower the interest rate slightly—.25%—and provide reassurance to potential lenders." We do not believe the Supreme Court of Appeals would approve of such an arrangement.

Our conclusion is bolstered by the expansive meaning that the Supreme Court of Appeals has given to the word "credit." The Court has explained that "[u]nquestionably, credit is that which enables one to enter into an obligation to be met in the future, but that is not the only meaning." *Sims*, 132 W. Va. at 842, 54 S.E.2d at 738. Rejecting a narrow reading of the word "credit," the Court has held that allowing municipalities to withdraw a sum each fiscal year from a special fund in the State Treasury is "a plain granting of credit" because the municipality may depend on the funds in planning future expenditures. *Id.* It has also concluded that providing space in a government building without cost is a granting of the State's credit. *State ex rel. State Bldg. Comm'n v. Casey*, 160 W. Va. 50, 56, 232 S.E.2d 349, 352 (1977); *see also* 53 W. Va. Op. Atty. Gen. 352 (1969) (concluding that a county board of education pledges the credit of the State by paying the tuition of out-of-state students); 45 W. Va. Op. Atty. Gen. 143 (1952) (concluding that a state university that pays all or part of the salary of a police officer employed by the City of Morgantown has granted the credit of the State). Were there any doubt about the application of Article X, Section 6 to the arrangement in question, we believe these cases put that doubt to rest.

Separately, we also think it likely that the Supreme Court of Appeals would find the contemplated arrangement to be a violation of Article X, Section 4 of the West Virginia Constitution. That provision states that "[n]o debt shall be contracted by this state, except to

meet casual deficits in the revenue, to redeem a previous liability of the state, to suppress insurrection, repel invasion or defend the state in time of war.” W. Va. Const. Art. X, §4. The Supreme Court of Appeals has taken a functional rather than formalistic approach to determining whether the State has incurred a debt in violation of Article X, Section 4. In *Winkler v. State School Building Authority*, 189 W. Va. 748, 434 S.E.2d 420 (1993), the Court concluded that the School Building Authority had unconstitutionally contracted a debt by issuing revenue bonds that were to be liquidated by legislative appropriations from the general fund, *even though the bonds stated that the State had no legal obligation to pay the bonds*. *Id.* at 760, 434 S.E.2d at 432. The challengers in that case specifically argued “that although future legislative appropriations may be used to pay for the bonds, it is clear from the language of the bonds themselves that there is no legal obligation requiring the Legislature to make such appropriations.” *Id.* at 759, 434 S.E.2d at 431. The Court expressly rejected that argument: “where the only source of funds for revenue bonds is general appropriations, it defies logic to say that the Legislature has no obligation to fund such bonds.” *Id.* at 761, 434 S.E.2d at 433. Looking to a case from the Ohio Supreme Court, the West Virginia high court determined that it “must examine a transaction not only for what it purports to be, but what it actually is.” *Id.* at 762, 434 S.E.2d at 434 (quoting *State ex rel. Ohio Funds Mgmt. Bd. v. Walker*, 561 N.E.2d 927, 932 (Ohio 1990)). The Court stressed that it could not “ignore the practical reality that will be visited upon a state’s credit if there is a default on the bonds.” *Winkler*, 189 W. Va. at 761, 434 S.E.2d at 433; *see also id.* at 763, 434 S.E.2d at 435 (“To accept the premise that the Legislature is not bound to fund the bonds and would allow a default, thereby impairing the credit rating of the State, assumes a naivete on our part that we simply do not possess.”).

For several reasons, we believe that *Winkler* would give the Supreme Court of Appeals a further ground to reject the contemplated arrangement.

First, although your letter states that the WVDE would not assume the county’s liability to the lender and that the agreement would include “an annual funding opt-out clause,” *Winkler* suggests that the Supreme Court of Appeals would take a functional view of the arrangement and conclude that it effectively creates an unlawful debt. *See also State ex rel. Clarksburg Mun. Bldg. Comm’n v. Spelsberg*, 191 W. Va. 553, 557, 447 S.E.2d 16, 20 (1994) (“In *Winkler* we concluded that the Court must look beyond the plain language of the agreement, and consider the practical consequences that will result when we determine whether the fiscal integrity of the State is unconstitutionally, or unlawfully compromised.”). Especially in light of the understanding that the State’s presence would result in a lower interest rate and “provide reassurance to potential lenders,” the “practical reality” is that failure to pay would impact the State’s credit and financial reputation. *See Winkler*, 189 W. Va. at 761, 447 S.E.2d at 433. Critically, the financial institution would have a security interest in the equipment and fixtures purchased by the loan, just as the bondholders in *Winkler* held an enforceable interest in the school buildings funded by the bonds. *See McGraw v. Caperton*, 191 W. Va. 528, 536 & n.7, 537, 446 S.E.2d 921, 929 & n.7, 930 (1994) (distinguishing the School Building Authority bonds in *Winkler* from a contract that created no security interest).

Second, the state aid to school districts from which the WVDE would repay the loan is appropriated by the Legislature from general revenue funds. W. Va. Code § 18-9A-1, -3. In *Winkler*, the Supreme Court of Appeals stressed the distinction between debts tied to a specific source of revenue and those intended to be paid off from the general fund. *Winkler*, 189 W. Va. at 757-58, 434 S.E.2d at 429-30 (explaining the “special fund doctrine” exception). Like the unlawful bonds in *Winkler*, the financial obligations discussed in your letter are intended to be repaid from general revenue funds.

Finally, as is true here, *Winkler* involved funds needed for the public educational system. The Supreme Court of Appeals began that case by acknowledging the “gravity of the bond issue in th[e] case, particularly since it relates to our public educational system.” *Id.* at 753, 434 S.E.2d at 425. Nevertheless, the Court struck down the bonds. *Id.* at 766, 434 S.E.2d at 438. Thus, while the funds at issue here may also be critical to educational needs, we do not believe that factor will cause the Court to distinguish *Winkler*.

* * *

Because we conclude that the Supreme Court of Appeals would likely find the contemplated arrangement a violation of two provisions of the West Virginia Constitution, we need not and do not address several other potential legal limitations, including one you suggest in your letter. For example, we do not opine on the applicability of West Virginia Code § 12-3-17, which prohibits “any state board, commission, officer or employee” from committing to pay funds in future fiscal years for which the Legislature has not yet made an appropriation. We do not assess whether the state aid formula established under West Virginia Code § 18-9A-1 to -22, which you reference in your letter, might limit the funds the WVDE could pay to a financial institution under the arrangement. Nor do we decide whether the contract described in your letter, which presumably would include the WVDE as a party, would have to comply with the requirements for state contracts. *See* W. Va. Code § 5A-3-10.

Sincerely,



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